

Three Secular Riddles



Rising Rates, Dollar Bull and the Transatlantic Alliance

Geneva, Zurich & Frankfurt

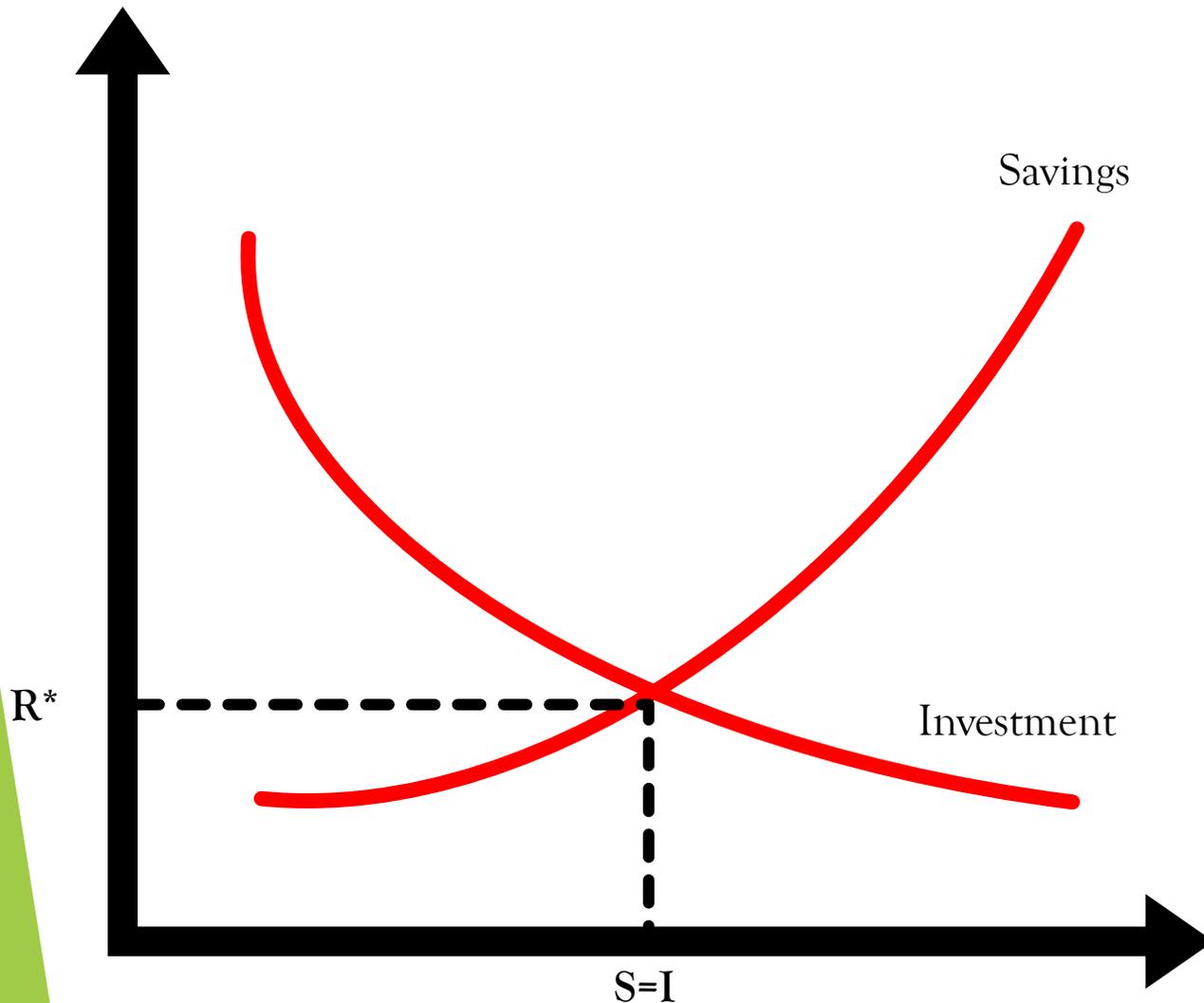
June 2018

Agenda



- **From a Savings Glut to a Savings Squeeze**
Higher for Longer ... Much Higher for Much Longer
- **Failing the Duck Test**
This Is Not What a Dollar Bull Looks Like
- **Le Divorce**
The End of the Transatlantic Alliance

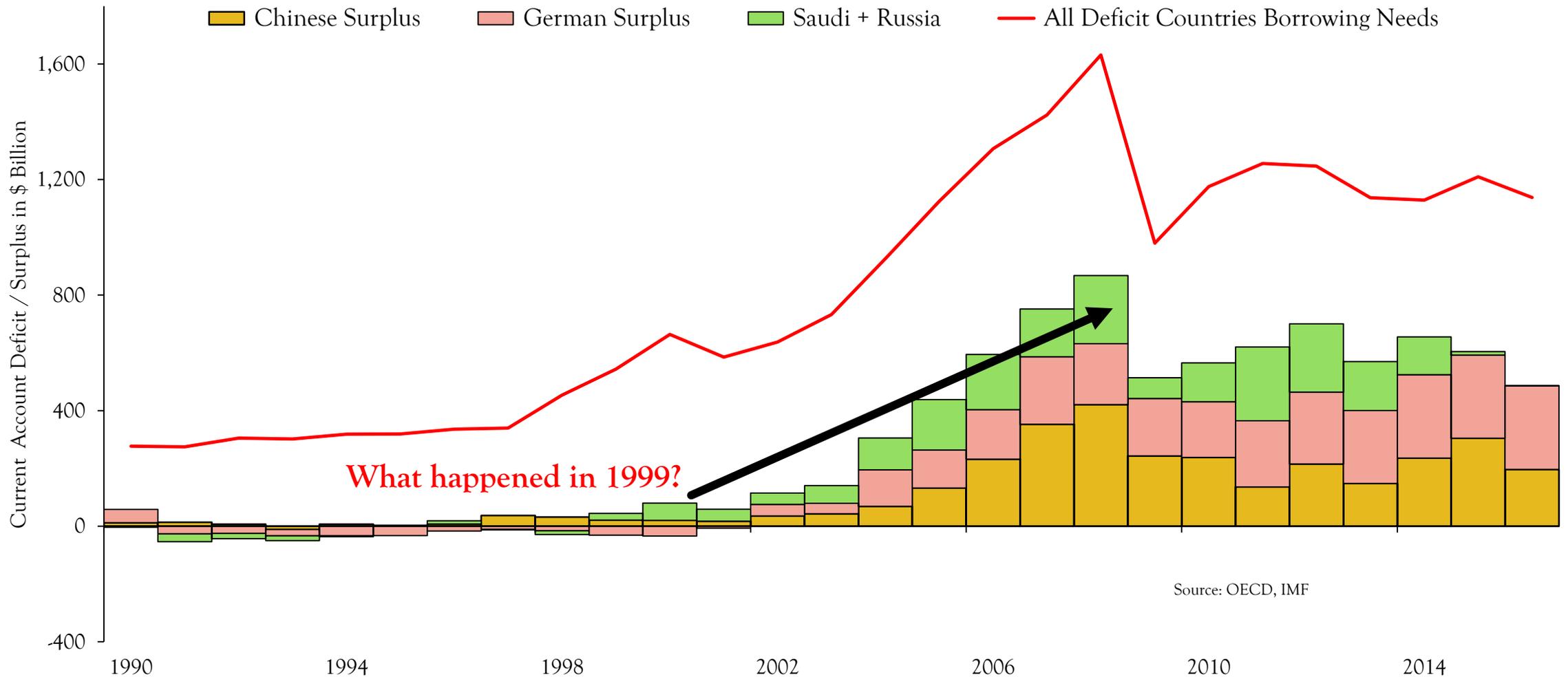
Understanding Interest Rates



- The interest rate is the price that clears the market for savings
 - From GDP accounting: $X-M = S-I$
 - Current account balances determines net savings
 - In global capital markets, the equilibrium interest rate is set so that: $I=S=X=M$
- If too many countries chase trade surpluses at the same time, excess savings will push interest rates down

The Triple Savings Glut of the 2000s-2010s

China, Germany, Russia and KSA accumulated \$8 trillion in excess savings since 1999



Source: OECD, IMF

What Happened in 1999?

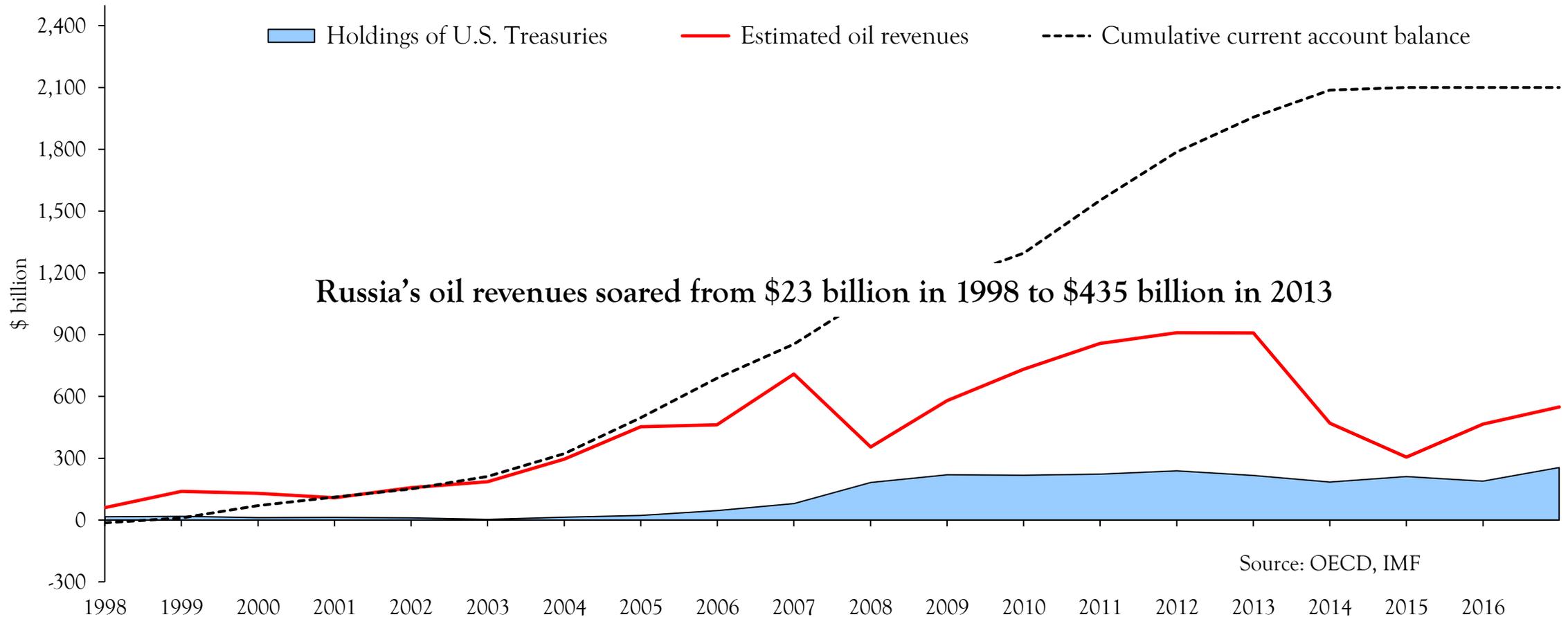
The triple shock of 1999

- January: the euro was launched, the Deutsche Mark is retired
→ World's largest exporter blessed with a weak currency
- August: Putin becomes Prime Minister as Brent prices recover from a secular low of \$9.6
→ Opec and Russia's oil revenues explode
- November: U.S.. China sign WTO agreement
→ China starts building \$4 trillion reserve hoard

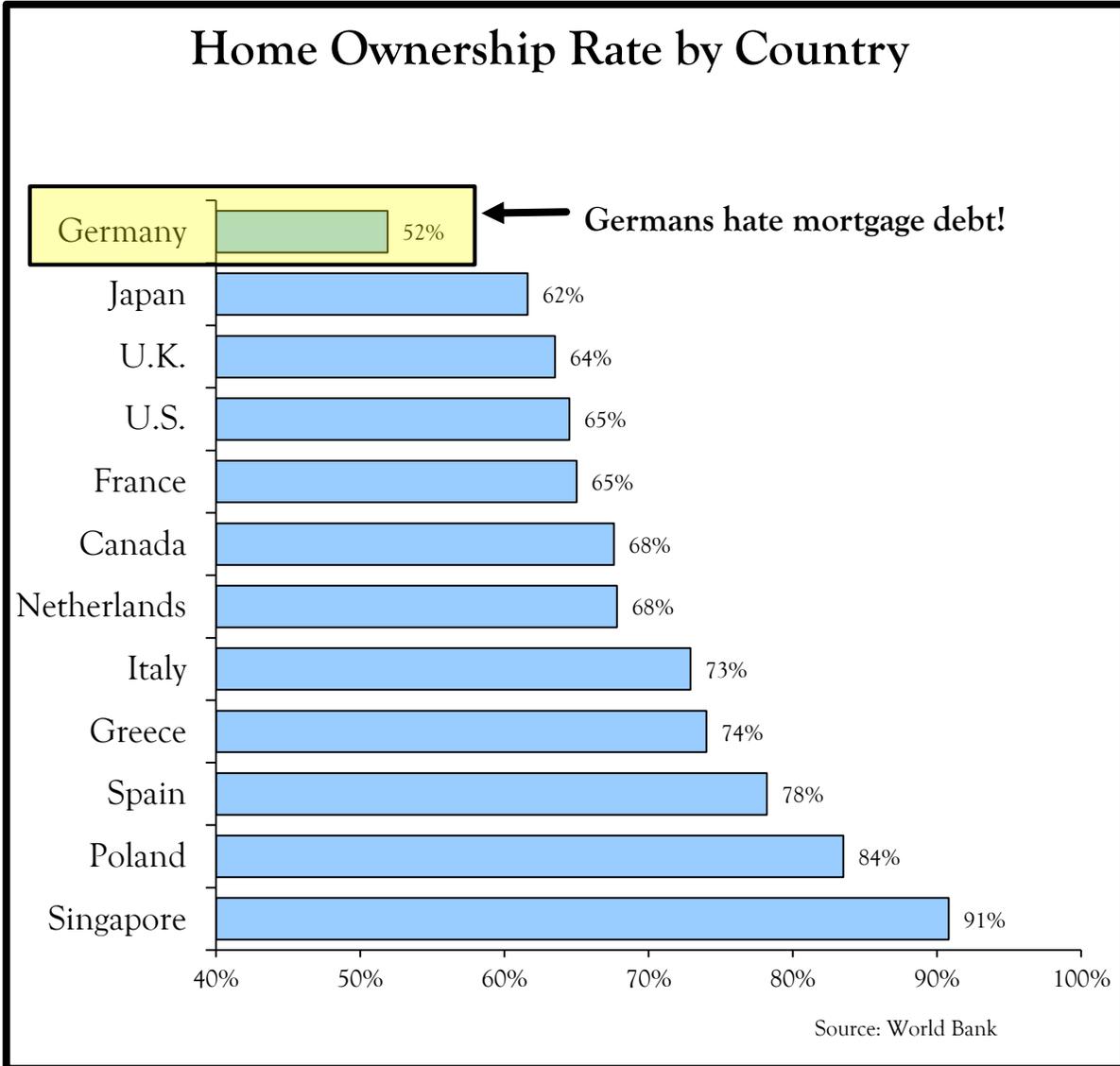
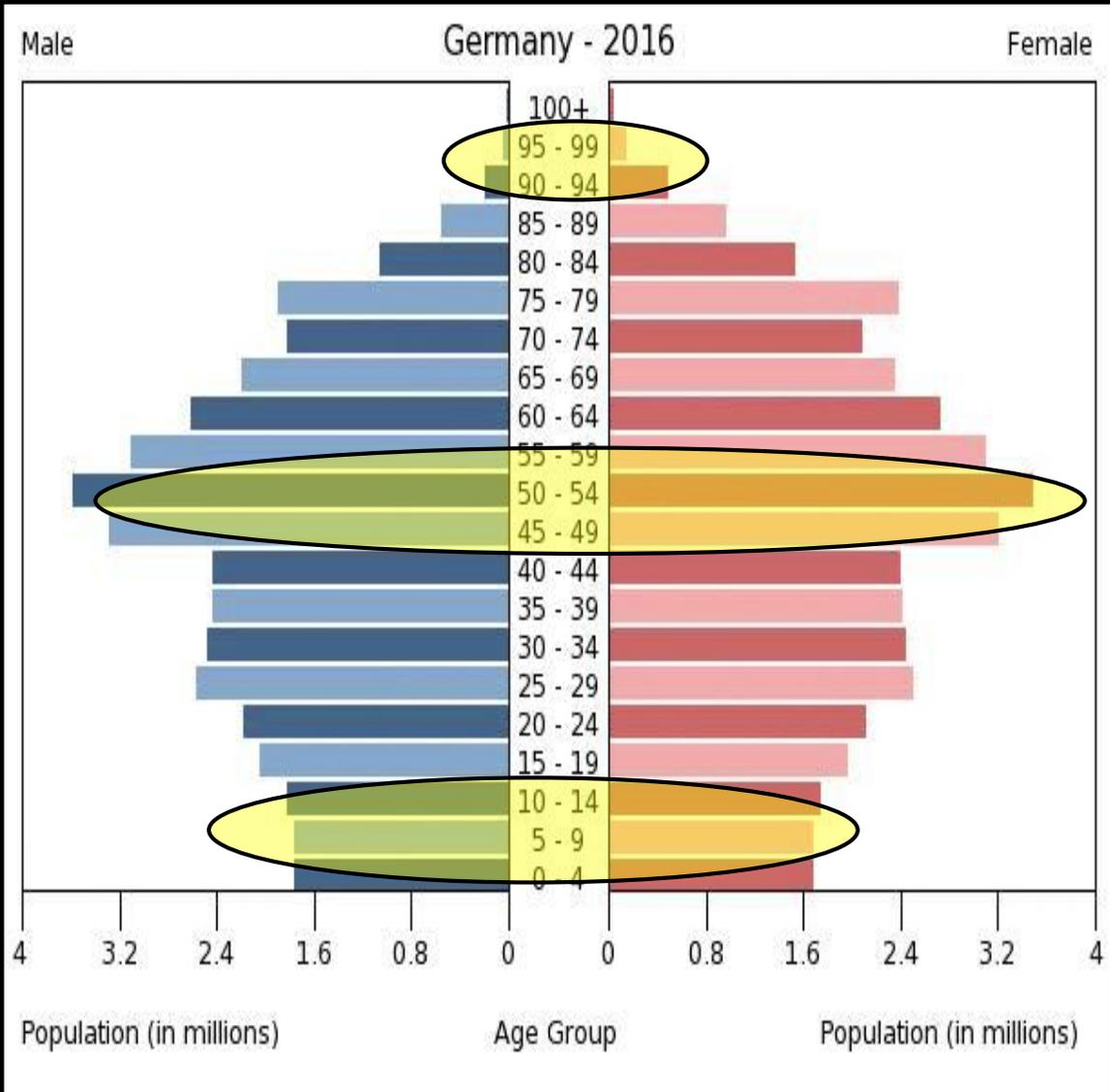


The Petrodollar Glut: \$2.1 Trillion

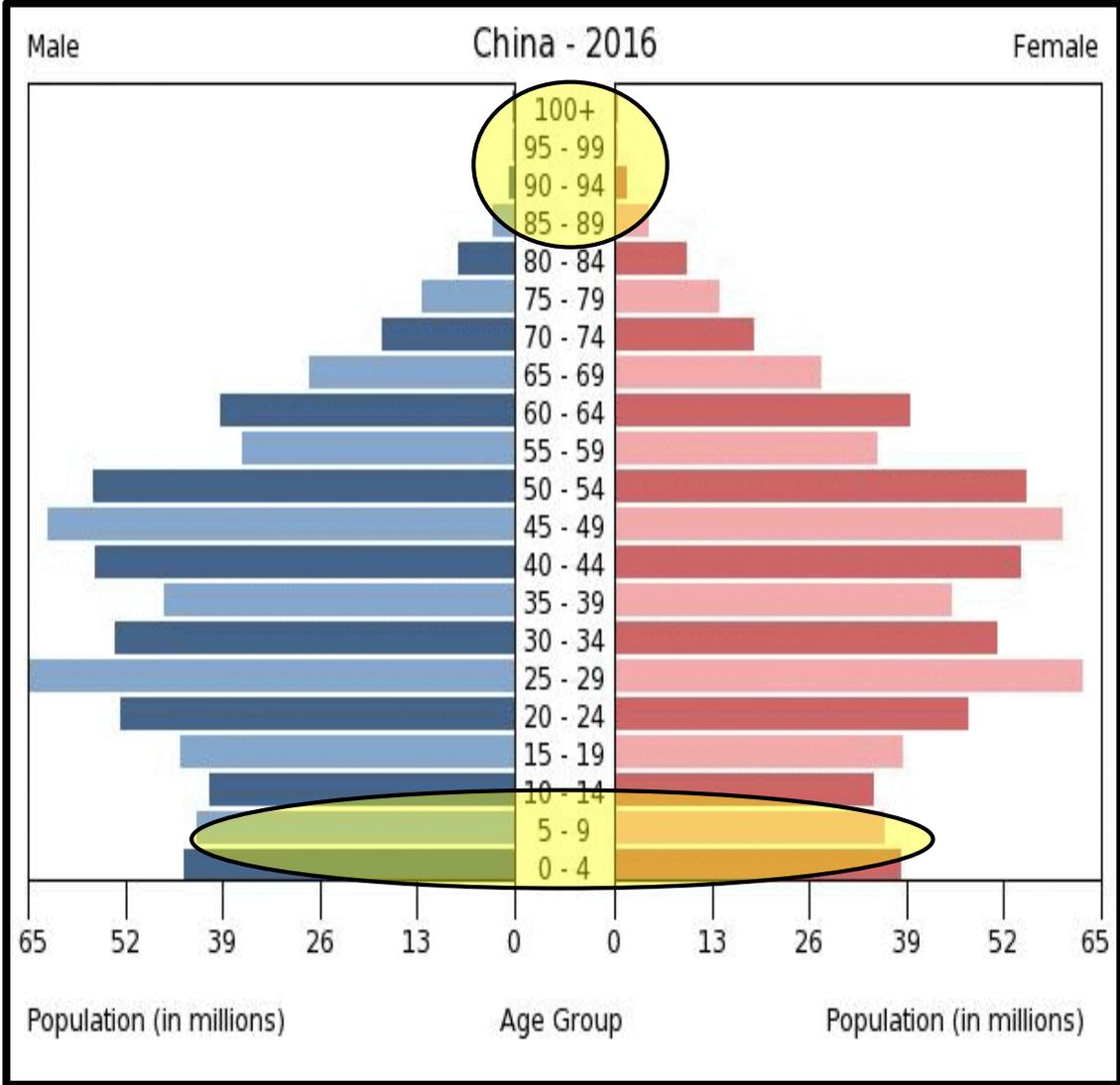
Russia and Saudi Arabia accumulated surpluses worth \$2.1 trillion since 1999



The German Glut: \$2.8 Trillion



The Chinese Glut: \$3.1 Trillion

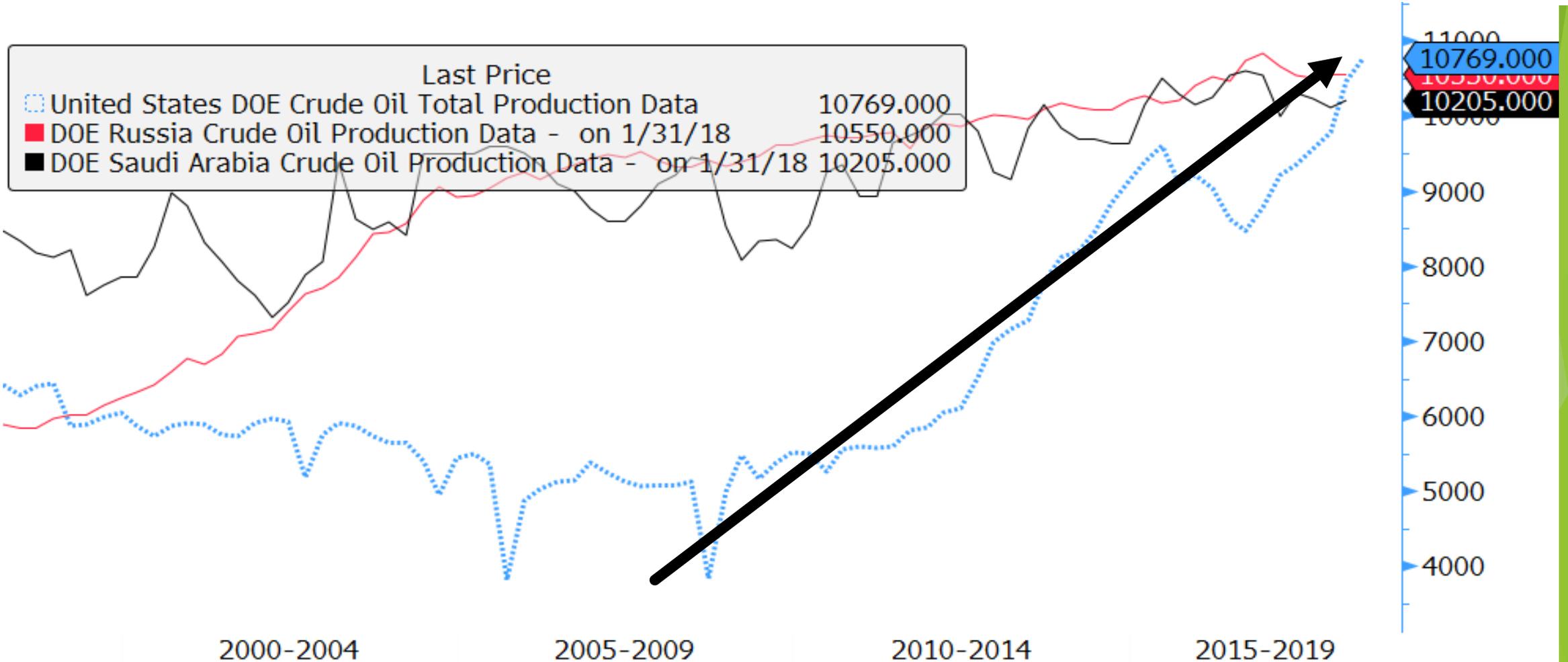


The day China decided to build a \$4 trillion reserve stash
The IMF's public shaming of Suharto , Jan 15 1998



The Great Savings Squeeze of 2018: OPEC

The U.S. Has Become the World's Top Producer of Oil in 2018



The Great Savings Squeeze of 2018: Germany

Auf Wiedersehen Balanced Budgets, Hallo Pension Shock

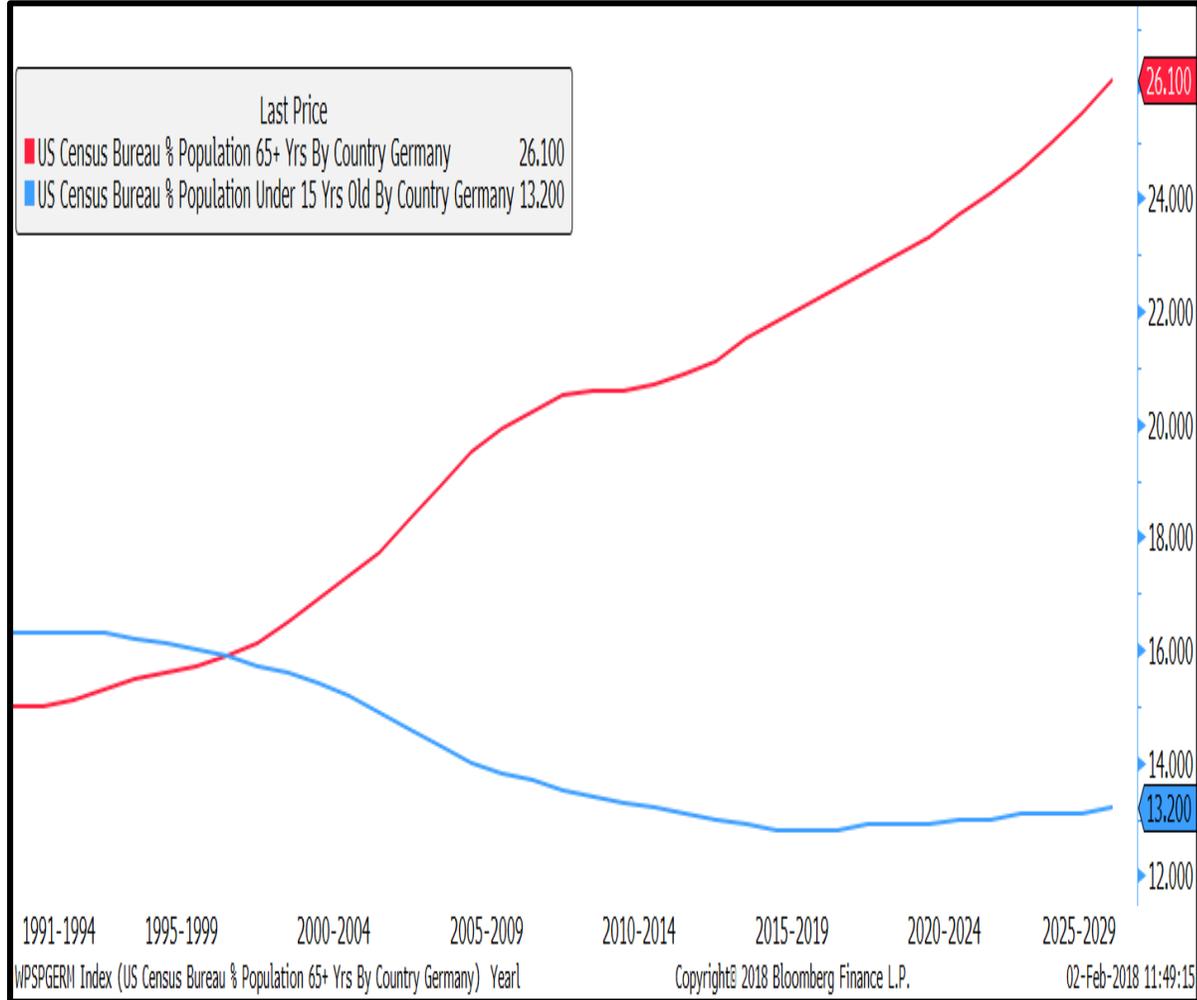


 **BMF** 
@BMF_Bund 

Auf Wiedersehen, Herr Minister! Ihre Kolleginnen und Kollegen im Bundesfinanzministerium. #Schäuble

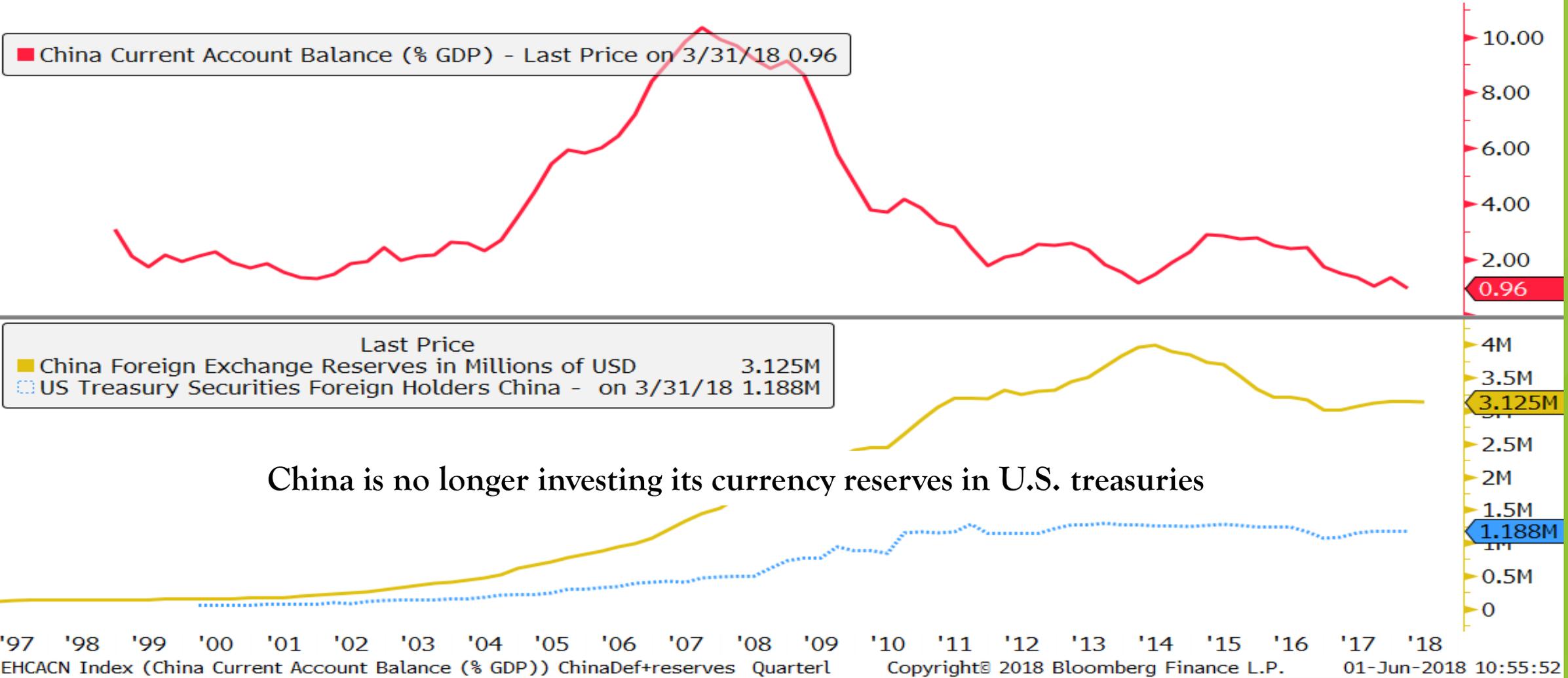
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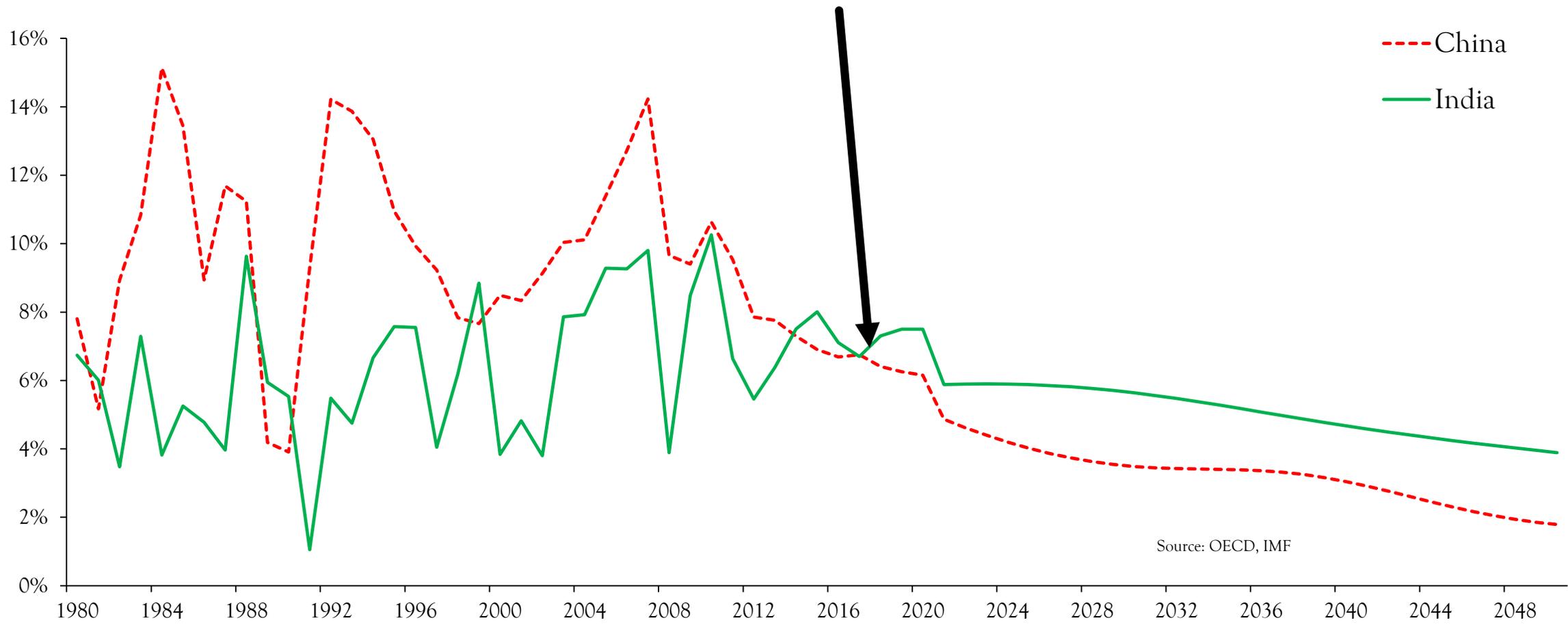
The Great Savings Squeeze of 2018: China

The Chinese Surplus Has Already Melted



The Great Savings Squeeze of 2018: China

India's growth should permanently overtake China's in 2018

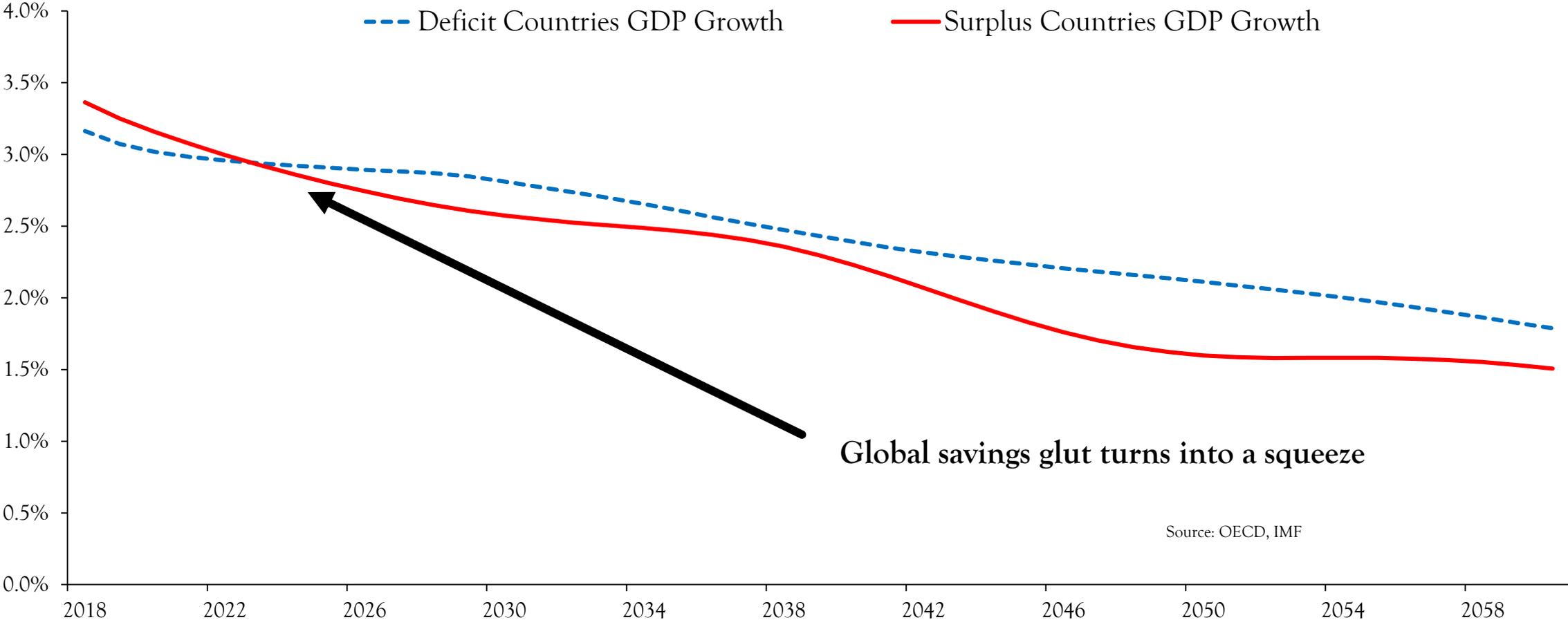


Source: OECD, IMF

The Great Savings Squeeze of 2018: World

Projected World Growth Rates

Based on OECD Long-Term Forecasts



Source: OECD, IMF

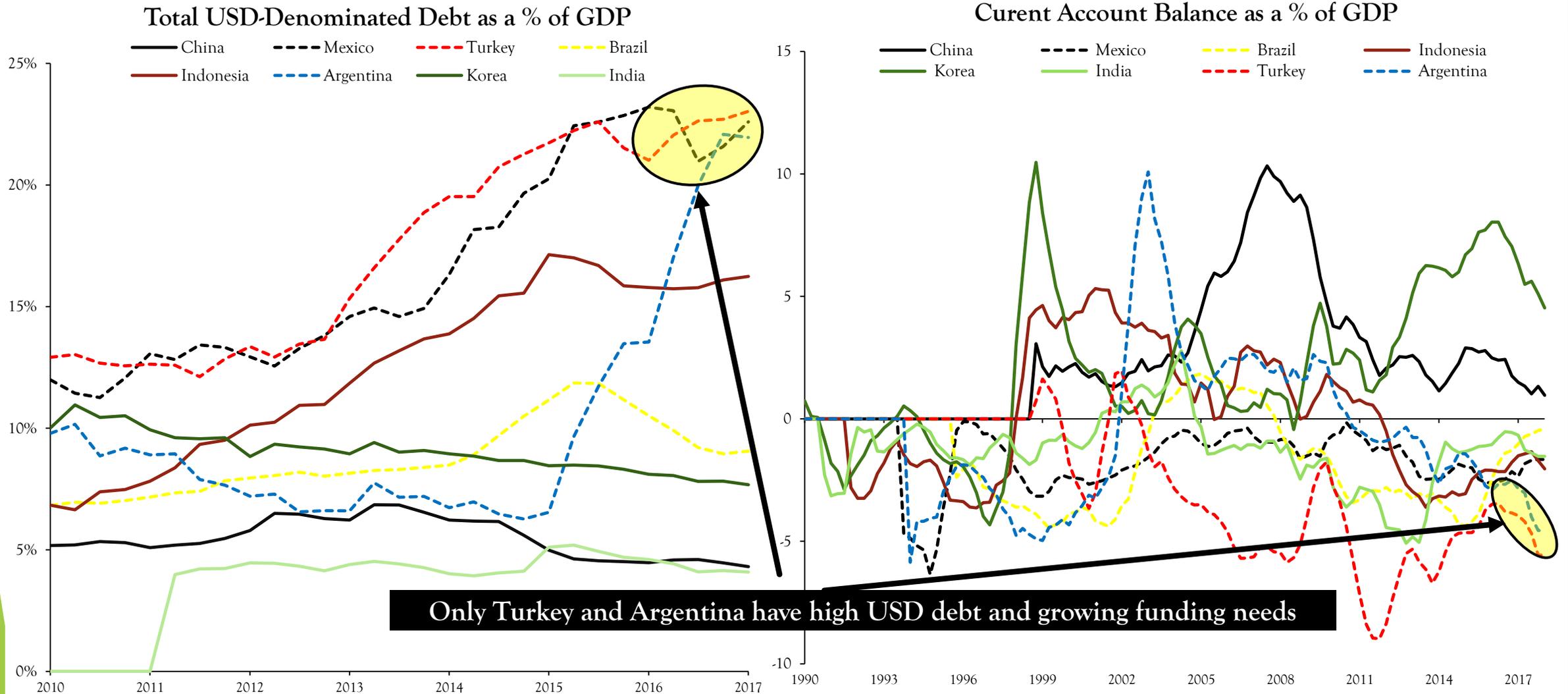
Failing the Duck Test: the (Fake) USD Rally

An Anatomy of Dollar Bull Markets

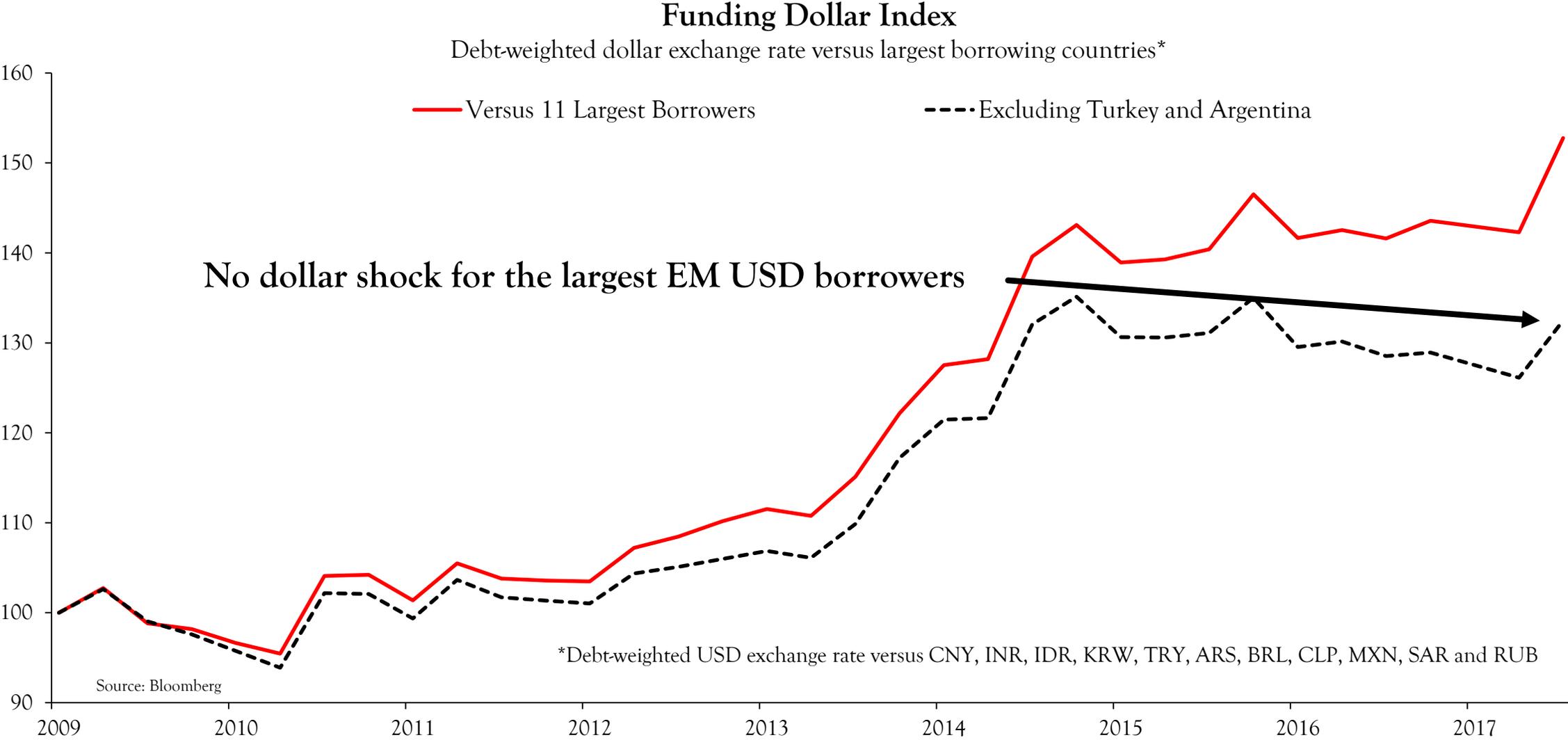
USD Dimension	Economic Metric	1980 to 1985 Cycle 95% Dollar Index Rally	1995 to 2002 50% Dollar Index Rally	2014 to 2016 31% Dollar Index Rally	2018?? 6.8% Dollar Index Rally
Domestic Currency of the United States	Change Inflation	-12.3 Percentage Point	- 2.2 Percentage Point	-0.1 Percentage Point	+ 0.4 Percentage Point
	Real Rate	+4.9%	+2.7%	-70 bp	-70 bp
	Real Growth Average	3.4%	3.4%	2.5%	2.6%
Funding Currency for EM	EM Sovereign Debt Crises and Defaults	Turkey, Argentina, Brazil, Chile, Uruguay, Egypt, Peru, South Africa	Venezuela, Thailand, Russia, Argentina, Indonesia	Argentina, Greece, Ukraine, Venezuela	Venezuela, Argentina, Turkey
Price of Commodities	Change in CCI Index	-28.8%	-17.3%	-25.0%	4.3%
	Change in Oil Prices	-35.9%	-37.5%	-49.5%	10.0%
Reserve Currency	Change in Gold Prices	-60.1%	-27.7%	-11.5%	-1.3%
	Share of USD in Official Foreign Reserves	N/A	Rose from 59% to 72%	Stable at 65%	??

The 2018 dollar rally fails the four parts of the secular bull market “duck test”
It is an accident due to a BOP crisis in Turkey and Argentina, and the Italian political crisis

A Contained EM Balance of Payments Crisis

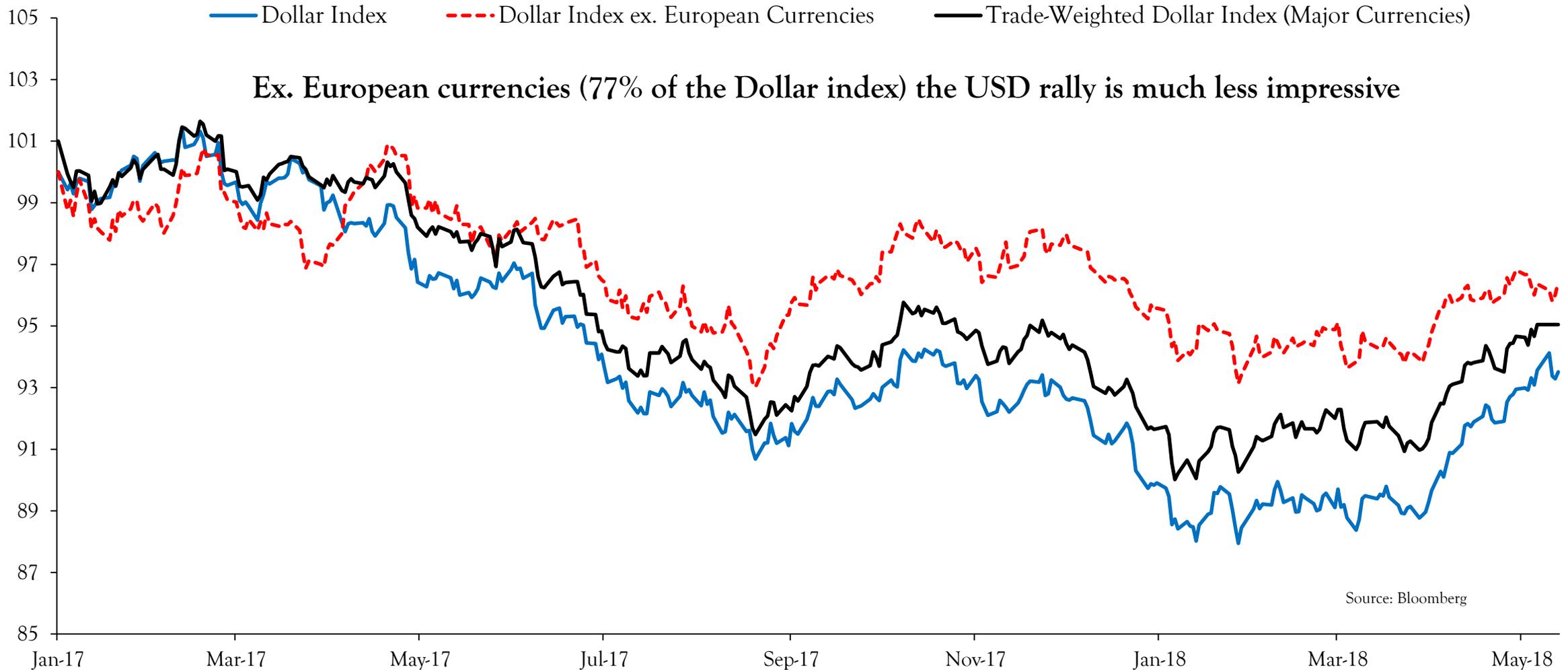


A Contained EM Balance of Payments Crisis



A (Mini) Euro Crisis

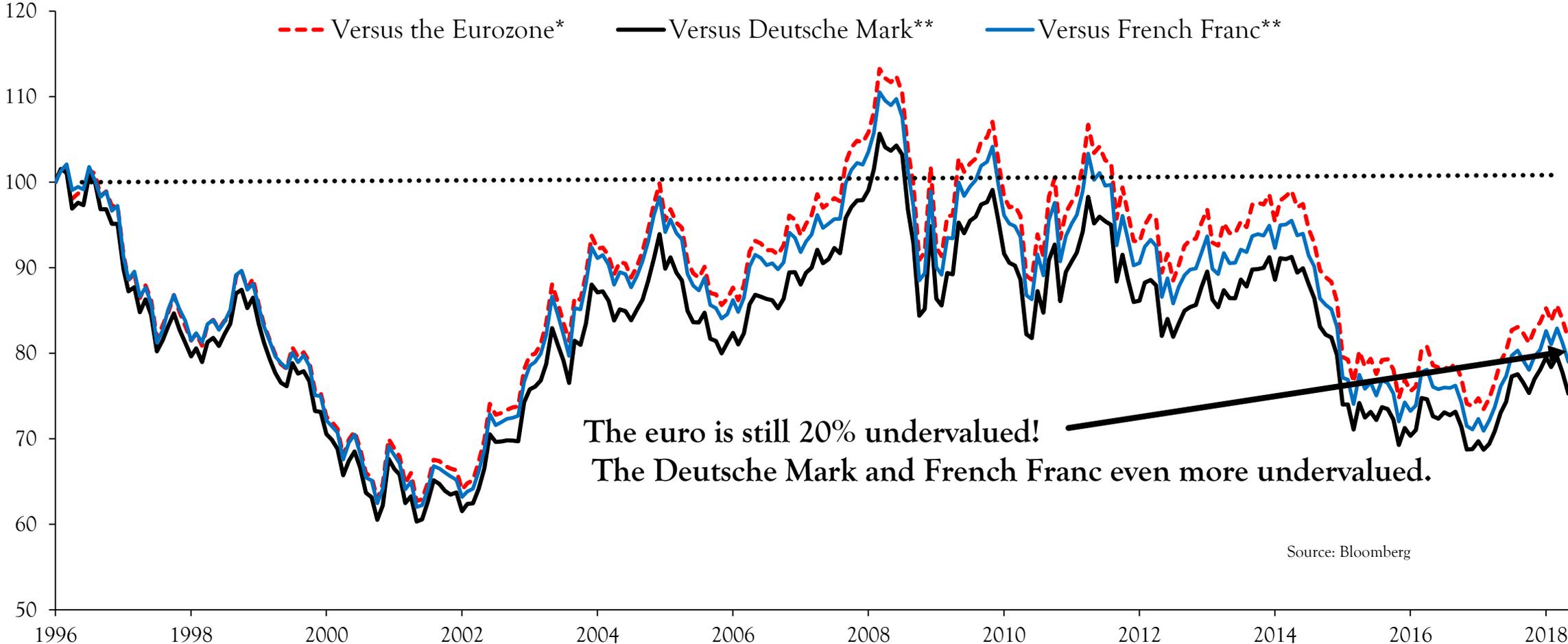
Dollar Index and Trade-weighted Dollar Index



A (Mini) Euro Crisis

Euro/Dollar Real Exchange Rate

100 = Jan 1996



Le Divorce: 4 Years of Humiliating Europeans

The Boomerang Effect

Sanctions on Russia Hit German Economy Hard

The United States and Europe last week announced the imposition of stronger sanctions against Russia in response to the ongoing crisis in Ukraine. German industry may be among the losers.

By Matthias Schepp and Cornelia Schmergal

Trump a signifié à l'ONU son retrait de l'accord de Paris sur le climat



European Banks' Post-Crisis Litigation Could Cost \$100 Billion

By Nicholas Comfort, Christian Baumgaertel and Hayley Warren
December 21, 2017

Iran nuclear deal: The EU's billion-dollar deals at risk

17 May 2018

f t m e Share

Germany braced for impact of US steel tariffs

Trade tension set to rise as exemption for EU is expected to expire next week

Donald J. Trump
@realDonaldTrump

We have a MASSIVE trade deficit with Germany, plus they pay FAR LESS than they should on NATO & military. Very bad for U.S. This will change

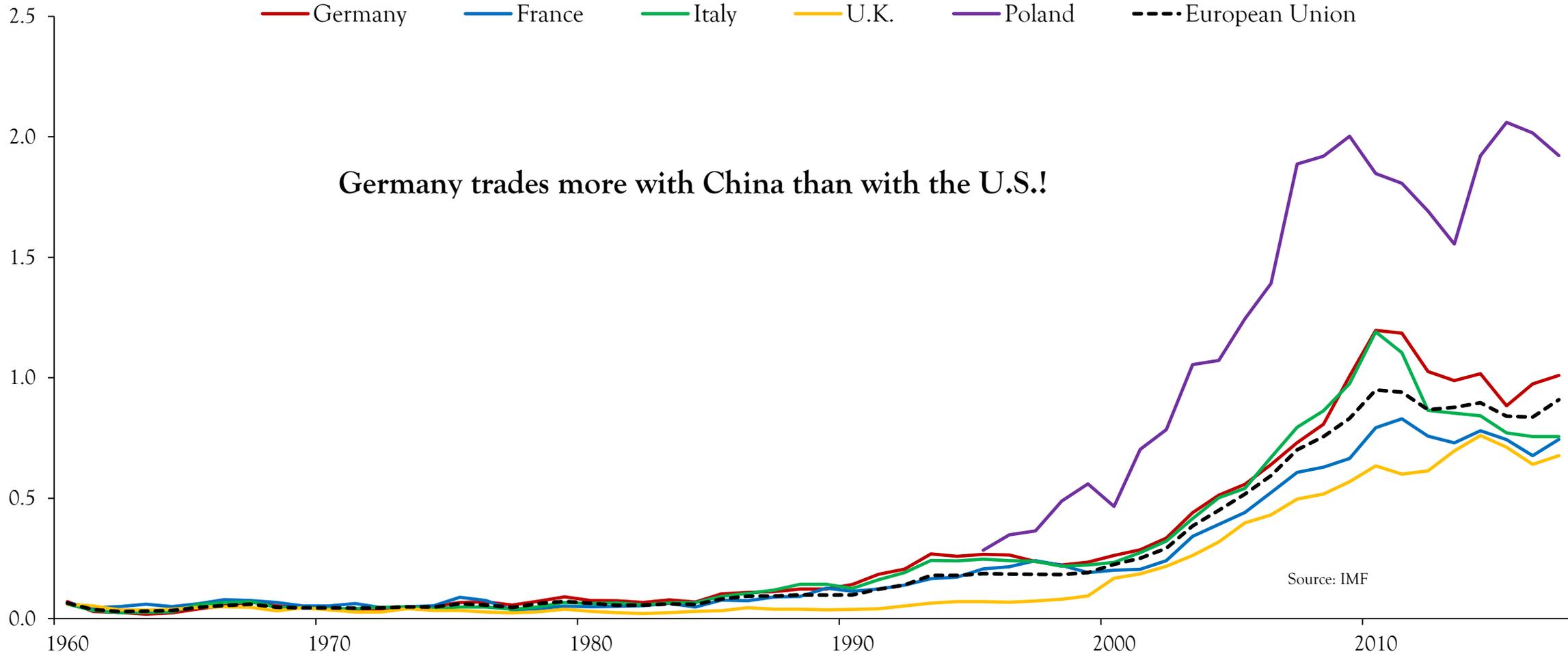
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85.4K 45.9K people are talking about this



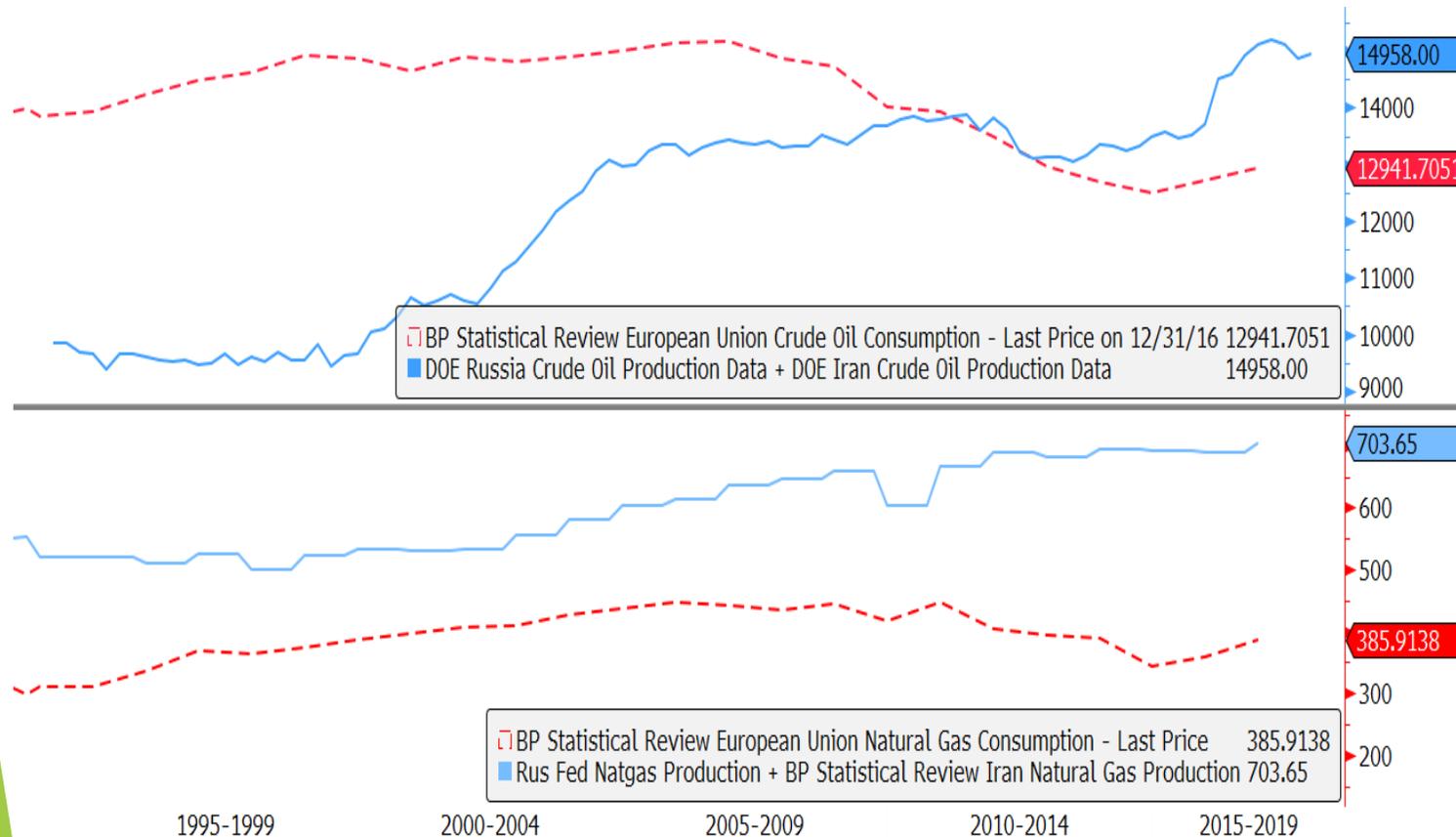
Le Divorce: Europe No Longer Needs the U.S. Alliance

Goods Trade with China as a % of the U.S. in Major European Countries



Le Divorce: Europe No Longer Needs the U.S. Alliance

Russia and Iran Could Supply All Europe's Energy By PIPELINE

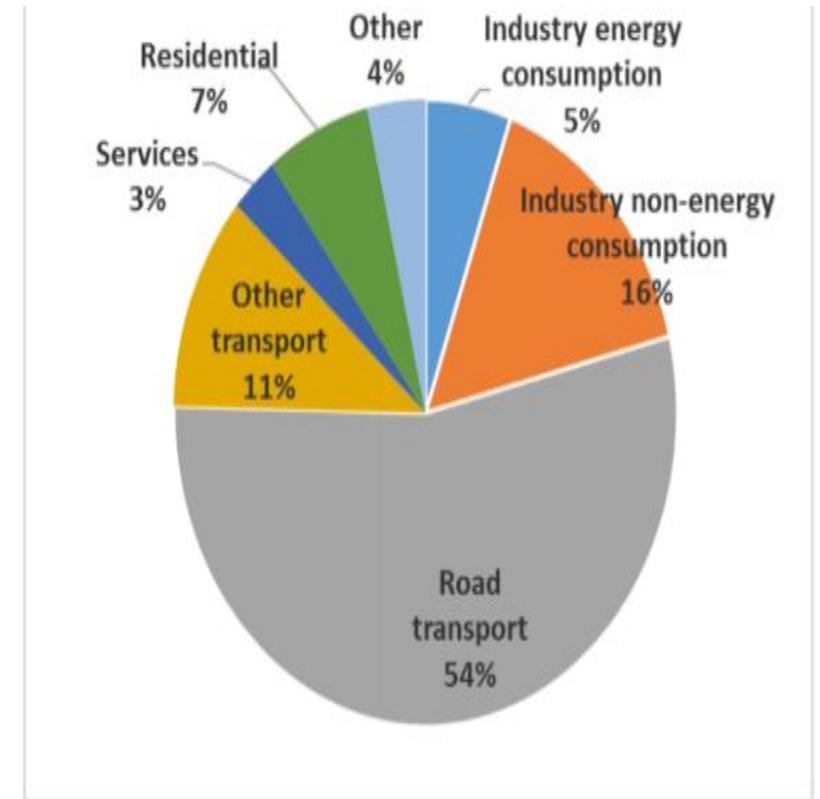


OCNERUN Index (BP Statistical Review European Union Crude Oil Consumption) EURU

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14-May-2018 11:31:59

EV revolution will reduce the EU's dependence on Middle East oil



Source: Eurostat Energy Balances

Conclusions

1. The savings glut is turning into a savings squeeze: rates will go higher for longer
2. The recent Dollar rally is an accident, not a trend
3. Europe and in the U.S. are growing apart
 - Shorten duration, raise cash
 - Short-term treasuries and variable rate bonds are safe place to hide
 - Options are still historically cheap: HEDGE!
 - Most Asian currencies offer high real rates and keep their value against USD
 - Euro should resume its rally in 2019 after the Italian crisis settles down
 - Favor “continental” European markets: France, Poland, Spain, Italy (in a few months)

Biography



Vincent is the global macro strategist for INTL FCStone Financial Inc, BD Division, where he authors weekly commentary on asset allocation, flows, Europe equities and quantitative topics. Prior to joining INTL FCStone Financial Inc., Vincent served as Europe Strategist for Ned Davis Research Group where he started the firm's European product. Vincent authored weekly publications on European markets, and designed proprietary trading models that combined fundamental, technical and macro indicators to identify major investment themes and market trends.

In November 2013, Vincent was awarded the Euromoney Padraic Fallon Editorial Prize for his in-depth study of the investment opportunities offered by the European debt crisis.

Prior to joining Ned Davis Research, Vincent was the Executive Vice President of TrimTabs Investment Research, where he headed the firm's quantitative research. At TrimTabs, Vincent authored weekly research reports on flows, sentiment, and European capital markets.

Vincent designed and traded large and profitable strategies based on supply and demand indicators for top-tier hedge funds.

He has been frequently quoted in the Financial Times, Wall Street Journal, Bloomberg, Forbes Magazine, and Barron's. Vincent was a subject matter expert on asset allocation for the level 3 of the CFA exam at the American College and he teaches Ethical and Professional Standards and Private Wealth Management for the CFA Society of San Francisco.

Vincent is a CFA charterholder. He completed a dual master's degree at Sciences-Po Paris (Cum Laude) and Columbia University and speaks English, French, Italian, and Indonesian.

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